TD/B/40(1)/12
TD/B/WG.1/8

UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

Report of the Ad Hoc Working Group on Investment and Financial Flows; Non-debt-creating Finance for Development; New Mechanisms for increasing Investment and Financial Flows on its second session

held at the Palais des Nations, Geneva,
from 28 June to 2 July 1993

UNITED NATIONS

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Geneva

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INTRODUCTION

1. The second session of the Ad Hoc Working Group on Investment and Financial Flows was held at the Palais des Nations, Geneva, from 28 June to 2 July 1993. In the course of the session, the Ad Hoc Working Group held two plenary meetings.

Chapter I

CONSIDERATION OF GLOBAL TRENDS AND ISSUES, INCLUDING FOREIGN INVESTORS' MOTIVATIONS

(Agenda item 2)

2. For its consideration of this item, the Ad Hoc Working Group had before it the following report by the UNCTAD secretariat:

"Foreign direct investment in developing countries: recent trends and policy issues" (TD/B/WG.1/7).

3. Contributions on foreign investors' motivations prepared by invited non-governmental experts and transmitted to the secretariat were circulated to the Ad Hoc Working Group in the miscellaneous documents series (TD/B/WG.1/Misc.2 and addenda) (see checklist of documents in annex II).

4. The secretariat had also prepared a selected bibliography on foreign direct investment (UNCTAD/GID/DF/3).

Seminar on Foreign Investors' Motivations held during the session

5. During the second session a two-day seminar-type discussion took place (item 2 of the agenda) led by invited panellists (see annex IV) who made presentations and answered questions from participants on the various topics as follows:

Topic 1. Traditional and new factors affecting foreign direct investment in developing countries and economies in transition;

Topic 2. The globalization of investment: consequences for developing countries and economies in transition;

Topic 3. The impact of host country policies on foreign investment decisions: the investors' viewpoint;

Topic 4. FDI in the 1990s: sectoral patterns and geographical distribution.

6. Following the presentations and discussions, the Chairman summed up the conclusions to be drawn, as follows:

(a) On traditional and new factors:

(i) The substantial increase in FDI flows to developing countries and countries in transition which had occurred recently had been the result of a large number of factors, including:

- A change of attitude in the host countries, which had welcomed FDI as a factor contributing to growth and efficiency;

- A change of attitude within companies themselves, which were working more closely with host countries on a partnership basis;

- An increase in global competition.

(ii) Several motives were involved in a firm's decision to invest abroad. These varied from firm to firm and sector to sector. They included the profit motive, safeguarding and gaining market shares, economies of scale, and a global competitive strategy.

(iii) Major factors influencing the location of FDI included the openness of the host economy, a fair and stable environment for FDI, domestic market potential, suitable export base, regional trading arrangements, availability of skilled labour, supportive infrastructure, and adequate domestic sourcing.

(iv) Among the traditional factors influencing FDI, it was felt that the low cost of unskilled labour was no longer a major determinant of FDI location.

(b) On globalization:

(i) Globalization had become a key feature of international economic relations, at the country level as well as at the firm level.

(ii) At the country level, almost all countries had opened their economies to the world. This was particularly true of the former centrally planned economies. At the firm level, globalization was an imperative for most firms, including small and medium-sized enterprises, under the pressure of global competition. Firms were increasingly applying global concepts to marketing, technology development, information systems, brands, market strategy and sourcing.

(iii) Globalization was reinforced by the close linkages between FDI and trade, notably through increased intra-firm trade and trade within regional groupings.

(c) On host countries policies:

(i) Host country policies had an important bearing on the flow of FDI. Favourable policies ranged from general economic policies leading to a stable macroeconomic framework and liberalization of domestic financial markets to specific FDI-related measures such as transparent and non-discriminatory legal and regulatory systems, and free transfer of profits and capital repatriation.

(ii) Among the impediments to FDI were sectoral protection, ceilings on foreign ownership, licensing and approval procedures, performance requirements and restrictions on employment of foreign staff.

(iii) Competition through the use of subsidies and incentives, particularly fiscal incentives, could be costly to developing countries. Where these already existed, their sudden removal might produce negative effects; where they did not as yet exist, their introduction might not produce the desired results. To the extent possible, developing countries should seek to avoid competitive bidding, enhance exchanges of information and promote transparency in order to reduce unnecessary costs.

(d) On FDI in the 1990s:

(i) The upward trend in FDI flows to developing countries and economies in transition was expected to continue in the 1990s, underpinned by competitive forces and further liberalization in these countries. However, constraints could emerge if economic uncertainty coupled with high unemployment in developed countries continued. These factors would increase further competition among countries, including developed countries, in attracting foreign direct investment.

(ii) FDI should not be regarded as the only engine of growth in host countries. However, it could play a very useful role in the transfer of technology and the upgrading of skills in developing countries, thereby contributing to their overall development.

Chapter II

CONSIDERATION OF HOST AND HOME COUNTRY POLICIES AND MEASURES TO PROMOTE FOREIGN DIRECT INVESTMENT, INCLUDING EXPORT PROCESSING ZONES AND SPECIAL ECONOMIC ZONES

(Agenda item 3)

7. For its consideration of this item, the Ad Hoc Working Group had before it the following report by the UNCTAD secretariat:

> "Export processing zones: role of foreign direct investment and developmental impact" (TD/B/WG.1/6).

8. The secretariat had also prepared a background study entitled:

> "Export processing zones: selected country experiences" (UNCTAD/GID/DF/2).

9. In addition, the country case studies transmitted to the secretariat were circulated to the Working Group in the miscellaneous documents series (TD/B/WG.1/Misc.3 and addenda) (see checklist of documents in annex II below).

A. Presentation of country case studies

10. Case studies were presented to the Ad Hoc Working Group by the following host countries: Brazil, China, India, Mexico, Morocco, Philippines and Republic of Korea as well as the following home countries: Netherlands, Republic of Korea, and United States of America. These presentations highlighted a number of elements common to the experience of many countries and led to an extensive discussion and exchange of views which the Chairman summed up as follows.

Host country policies

11. The Working Group noted that most countries had embarked on wide-ranging economic reforms and on the liberalization of their economic policies in general, and of their policies towards FDI, in particular. The pace of liberalization varied considerably among countries, ranging from gradualism to shock treatment. For some countries, liberalization had helped to increase FDI inflows; for others, especially the least developed countries, despite bold economic reforms, FDI did not flow in as expected. In many countries, some sectors, such as financial services, were still protected from foreign investment. Access to these sectors was restricted for a number of reasons, including strategic factors and protection of national infant industries. However, most countries were reducing sectoral protection considerably.

12. The trend towards regionalism was widely discussed. It was generally felt that the formation of regional trading groupings would have an important impact on the FDI pattern. In the foreseeable future, countries outside the regional groupings might be at a disadvantage in attracting FDI.

13. On the contribution of FDI to host countries' development and competitiveness, the Working Group noted that FDI played an important role in

the industrialization process. However, some countries were concerned about the low level of large-scale FDI and FDI in high-technology sectors flowing to them.

14. An extensive discussion took place on the role of incentives and performance requirements. Many countries had eliminated performance requirements, although others had maintained some to support development. Reliance on incentives was mostly used to promote priority sectors or to enhance the development of particular regions. In some countries, performance requirements or incentives were applied on a "national treatment" basis, that is, national and foreign enterprises were treated equally in this regard.

Home country policies

15. In the discussion of home country case studies, the importance of an open and liberal policy by host countries with regard to FDI from home countries was underlined. Governments of home countries had adopted various measures to encourage FDI in developing countries and countries in transition.

16. Widely used instruments were bilateral investment and protection agreements. These contained rules on fair and equitable treatment, free transfer of payments related to the investment, and international arbitration in case of disputes.

17. In addition, home countries had developed instruments to reduce perceived risks of FDI in developing countries and countries in transition. Mention was made of subsidies for feasibility studies, and of re-insurance of investments against political risks. With regard to the latter, experiences varied considerably among countries, depending on investment patterns and business culture.

B. Export processing zones

18. The representative of the UNCTAD secretariat introduced its report TD/B/WG.1/6 on export processing zones (EPZs), noting that there had been a rapid expansion of such zones during the last two decades. The principal objective in setting up EPZs was to promote export-oriented industrialization. Specifically, the aim was to enhance growth prospects by attracting foreign capital, providing new employment opportunities, increasing foreign exchange earnings, promoting the transfer of technology, and developing linkages with the domestic economy. Among the issues raised were how to assess the efficiency of EPZs, and how to create forward and backward linkages with the domestic economy, improve the transfer of technology, find an appropriate private/public sector mix, and address social concerns.

19. Among the points discussed by the Working Group were the following:

- As had been indicated by many country studies, despite some failures, EPZs had largely met their objectives by attracting FDI, creating employment and increasing exports. A good location was important for the success of an EPZ;

- Backward and forward linkages had not in general developed to a significant degree, but in some cases, such as in the special economic zones, linkages had been strengthened;

- Despite the growing trend toward trade liberalization, there was still a role for EPZs to play. EPZs could serve as windows for attracting FDI and for introducing market reforms gradually. They likewise had an important demonstration effect and could be used to promote new activities.

Chapter III

ORGANIZATIONAL MATTERS

A. Opening of the session

20. The second session of the Ad Hoc Working Group was opened on 28 June 1993 by the Chairman, Mr. J.P. Huner.

B. Bureau of the Ad Hoc Working Group at its second session

21. At its 3rd (opening) plenary meeting on 28 June 1993, the Working Group elected Messrs. F.A. Gomes (Brazil) and R. Krzysków (Poland) as Vice-Chairmen, to replace Messrs. L. Amaral Lopez (Brazil) and J. Stypa (Poland) who were unable to attend the second session. Accordingly, the Bureau of the Ad Hoc Working Group at its second session was constituted as follows:

Chairman:	Mr. J.P. Huner (Netherlands)
Vice-Chairmen:	Mr. M.M. Rahman (Bangladesh) Mr. F.A. Gomes (Brazil) Mr. G. Blehy (Côte d'Ivoire) Mr. R. Krzysków (Poland) Mr. R.G. McGrath (United States of America)
Rapporteur:	Mr. R. Serrano (Mexico)

C. Adoption of the agenda and organization of work

(Agenda item 7)

22. At the same meeting, the Ad Hoc Working Group adopted the provisional agenda for the second session as approved by the Ad Hoc Working Group at its first session and circulated by the secretariat in TD/B/WG.1/5. The agenda for the second session reads as follows:

1. Adoption of the agenda and organization of work

2. Consideration of global trends and issues, including foreign investors' motivations

3. Consideration of host and home country policies and measures to promote foreign direct investment, including export processing zones and special economic zones

4. Provisional agenda for the third session of the Ad Hoc Working Group

5. Other business

6. Adoption of the report of the Working Group to the Board.

23. The Working Group also broadly endorsed the suggested organization of work set out in the annex to TD/B/WG.1/L.5, subject to clarifications of detail made by the Chairman.

D. Provisional agenda for the third session of the Working Group

(Agenda item 4)

24. At its 4th (closing) meeting on 2 July 1993, the Ad Hoc Working Group approved the provisional agenda for its third session, as set out in TD/B/WG.1/L.5 (see annex I below for the provisional agenda).

25. The Ad Hoc Working Group decided to recommend that its third session should be held from 10 to 14 January 1994.

E. Adoption of the report of the Ad Hoc Working Group to the Board

(Agenda item 6)

26. At the same meeting, the Ad Hoc Working Group adopted the draft report on its second session (TD/B/WG.1/L.4) and authorized the Rapporteur to complete the final report as appropriate.

Annex I

PROVISIONAL AGENDA FOR THE THIRD SESSION OF
THE AD HOC WORKING GROUP

1. Adoption of the agenda and organization of work

2. Consideration of host and home country policies to promote foreign direct investment

3. Multilateral measures to promote foreign direct investment

4. Portfolio equity investment and new financing mechanisms

5. Provisional agenda for the fourth session of the Ad Hoc Working Group

6. Other business

7. Adoption of the report of the Ad Hoc Working Group to the Board.

Annex II

CHECKLIST OF DOCUMENTS

Symbol	Title	Languages
	A. Pre-sessional documents	
TD/B/WG.1/5	Provisional agenda and annotations to the provisional agenda	A/C/E/F/R/S
TD/B/WG.1/6	Export processing zones: Role of foreign direct investment and development impact	A/C/E/F/R/S
TD/B/WG.1/7	Foreign direct investment in developing countries: Recent trends and policy issues	A/C/E/F/R/S
	B. Non-sessional documents	
Contributions by invited experts:		
TD/B/WG.1/Misc.2	- Mr. F.A. Maljers, UNILEVER	English
TD/B/WG.1/Misc.2/Add.1	- Mr. Helmut O. Maucher, Chairman of the Board and Chief Executive Officer, Nestlé	English
TD/B/WG.1/Misc.2/Add.2	- Mr. Giacomo Luciani, ENI	English
TD/B/WG.1/Misc.2/Add.3	- Ms. Debora L. Spar, Assistant Professor of Business Administration, Harvard University	English
TD/B/WG.1/Misc.2/Add.4	- Ms. Grazia Ietto-Gillies, Professor of Applied Economics South Bank University	English
TD/B/WG.1/Misc.2/Add.5	- Mr. J.-L. Le Bideau Principal Officer Directorate for Financial, Fiscal and Enterprise Affairs Organisation for Economic Cooperation and Development, Paris, France	French

Symbol	Title	Languages
Case studies prepared by member countries:		
TD/B/WG.1/Misc.3	- Netherlands	English
TD/B/WG.1/Misc.3/Add.1	- Mexico	English
TD/B/WG.1/Misc.3/Add.2	- Republic of Korea	English
TD/B/WG.1/Misc.3/Add.3	- India	English
TD/B/WG.1/Misc.3/Add.4	- Philippines	English
TD/B/WG.1/Misc.3/Add.5	- China	English
TD/B/WG.1/Misc.3/Add.6	- Brazil	English
TD/B/WG.1/Misc.3/Add.7	- United States of America	English
TD/B/WG.1/Misc.3/Add.8	- Morocco	French

C. Background documents prepared by the UNCTAD secretariat

UNCTAD/GID/DF/2	Export processing zones: selected country experiences	English
UNCTAD/GID/DF/3	Selected bibliography on foreign direct investment	English

Annex III

MEMBERSHIP AND ATTENDANCE a/

1. The following States members of UNCTAD, members of the Ad Hoc Working Group, were represented at the session:

Argentina
Austria
Bangladesh
Belgium
Brazil
Bulgaria
China
Colombia
Cuba
Denmark
Egypt
France
Germany
Greece
Hungary
India
Indonesia
Iran (Islamic Republic of)
Italy
Japan
Lebanon
Mexico
Morocco
Myanmar
Netherlands
Nigeria
Norway
Pakistan
Philippines
Poland
Portugal
Republic of Korea
Romania
Russian Federation
Senegal
Slovakia
Spain
Switzerland
Thailand
United Kingdom of Great Britain and Northern Ireland
United Republic of Tanzania
United States of America
Venezuela
Zimbabwe

2. The following other States members of UNCTAD, not members of the Ad Hoc Working Group, were represented as observers at the session:

Cameroon
Ecuador
El Salvador
Ethiopia
Madagascar
Nepal
Qatar
Uruguay

3. The Economic and Social Commission for Asia and the Pacific was represented at the session.

4. The following specialized and related and related agencies were represented at the session:

International Labour Organisation
International Monetary Fund
United Nations Industrial Development Organization

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a/ For the list of participants, see TD/B/WG.1/INF.2.

5. The following intergovernmental organizations were represented at the session:

European Community
Organization for Economic Co-operation and Development

6. The following non-governmental organizations were represented at the session:

General Category

International Chamber of Commerce
World Federation of United Nations Associations

Special Category

International Association of Islamic Banks

Annex IV

LIST OF PANELLISTS

Topic 1. Traditional and new factors affecting foreign direct investment in developing countries and economies in transition

Panellists:

Mr. H. Oberhänsli
Assistant to the Chairman for Economic Affairs
Nestlé S.A.
Vevey, Switzerland

Mr. D. Hepburn
Unilever
London, United Kingdom

Mrs. G. Ietto-Gillies
Professor of Applied Economics
South Bank University
London, United Kingdom

Topic 2. The globalization of investment: consequences for developing countries and economies in transition

Panellists:

Mr. J. Charlton
Managing Director
Chase Manhattan Bank
New York, N.Y.
United States of America

Ms. D. Spar
Assistant Professor of Business Administration
Harvard University
Boston, Massachusetts
United States of America

Mr. P. Mountfield
Executive Secretary
Development Committee
Washington, D.C.
United States of America

Topic 3. The impact of host country policies on foreign investment decisions: the investors' viewpoint

Panellists:

Mr. H. Stordel
Economic Research Department
Crédit Suisse
Zurich, Switzerland

Mr. H. Oberhänsli
Assistant to the Chairman for Economic Affairs
Nestlé S.A.
Vevey, Switzerland

Mr. F. Fornasari
Director, Trade and Investment Unit, International Relations
FIAT s.p.a.
Turin, Italy

Mr. G. Kume
Chief Representative
Japan Eximbank
Paris, France

Mr. J.-L. Le Bideau
Principal Administrator
Directorate for Financial, Fiscal and Enterprises Affairs
Organisation for Economic Cooperation and Development
Paris, France

Topic 4. FDI in the 1990s: sectoral patterns and geographical distribution

Panellists:

Mrs. G. Ietto-Gillies
Professor of Applied Economics
South Bank University
London, United Kingdom

Mr. G. Luciani
Deputy Director
International Analysis, ENI
Rome, Italy

Ms. D. Spar
Assistant Professor of Business Administration
Harvard University
Boston, Massachusetts
United States of America

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Printed at United Nations, Geneva
GE.93-52464 - August 1993 - 3,590

United Nations publication